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CAPITALIZATION OF THE UNITED STATES STEEL CORPORATION.

THE surplus earnings of the United States Steel Corporation for the first six months of its existence exceeded $12,000,000. It is confidently asserted that the second half-yearly statement, to be issued in March, 1902, will be even more favorable. Thus far the enterprise is more than fulfilling the predictions of its promoters, that dividends could be maintained on both preferred and common stock. These large earnings are the result of productive advantages which have been so often enumerated and described that the briefest survey, by way of introduction to the present discussion, will suffice. The United States Steel Corporation controls 80 per cent. of the supply of iron ore at the head of Lake Superior. It owns practically the whole of that portion of the Connellsville coking coal field not yet exhausted. It owns the boats and railroads by means of which the crude materials of steel production are brought together. The plants of the Corporation are located at the points of largest present advantage, where materials can be most economically assembled and from which markets can be most easily reached. These plants include approximately 70 per cent. of the productive capacity of the United States, taking the total output of all forms of steel products as the basis of estimate. The policies of the company are directed by the most able men in the steel industry, and its financial support includes the strongest houses in the United States. The result of these advantages is production and distribution at a lower cost than has ever been reached by any company engaged in the manufacture of steel. Minimum expenses of production combine with heavy demands for product and high-selling prices to produce the huge sum of profits which has been mentioned, and out of which such liberal dividends have been paid.

These profits, however, although enormous, are none too large for the requirements of investment security. Net earnings of $125,000,000 give an annual surplus of $40,000,000, or 2.8 per cent. on the total capitalization of the company. At this rate, in five years, providing that conditions of capital and income remained unchanged, a surplus of 14 per cent. will have been accumulated, and the common stock will be entitled to rank as an investment security. A more conservative management would refuse to pay dividends on the common stock until a considerable surplus had been accumulated; but the United States Steel Corporation was definitely committed from the start, not only by the announcement of its prospectus, but by the practice of most of its constituent companies, to a policy of liberal disbursement. And, having once been begun, this policy can be abandoned only at a sacrifice of security values which would entail heavy losses upon the stockholders and injure the reputation of the principals. The necessity for the payment of dividends arises, also, from the existence of the cumulative provisions which appear in the contract with the holder of the preferred stock. If the stock of the United States Steel Corporation were all of one issue, or if the cumulative feature did not attach to the preferred stock dividends, no dividends need be paid for the current year, and $95,000,000 could be added to surplus reserve. Given another year as profitable as 1901 has been, and the Corporation would have accumulated a reserve fund of 20 per cent., and would then be able to guarantee a fixed return to its stockholders. The cumulative provision, however, enforces the necessity of the payment of 7 per cent. dividends on its preferred stock; and this payment requires a yearly appropriation out of earnings of $35,649,924. Failing in the payment of any part of this sum, the deficit remains as a preferred claim against earnings; and this must be satisfied before the resumption of dividends on the common stock. In justice to the holder of common stock, therefore, preferred dividends, when earned, must be paid out. Payment of dividends on one class of securities, moreover, is a presumption in favor of disbursements to the junior issues; and finally, as before remarked, the steel combine is definitely committed to a policy of dividend payment. In considering the financial position of the steel trust, therefore, we must understand by this term the ability of the steel trust to pay dividends.

We start from a basis of fixed charges of $65,068,924, divided as follows: sinking funds and maintenance, $14,119,000; interest on bonds, $15,200,000; dividends on preferred stock, $35,649,924. If the reputation and policy of the company demand the payment of dividends on the common stock as a condition of financial stability, the total requirements are increased to $85,255,858, which must be earned before any surplus can be accumulated. Do the past history and present circumstances of the iron and steel trade, and, in particular, the situation of the United States Steel Corporation in reference to cost of production and market control, warrant the conclusion that this sum can be provided, and at the same time an adequate surplus reserve accumulated?

In the November number of the *Quarterly Journal of Economics*, under the title "The Integration of Industry in the United States," Dr. W. F. Willoughby presented conclusive evidence of the existence of a tendency in the industrial world towards the uniting of all the factors of production in particular lines into single companies, each of which owns or controls the source of its own supply of materials and markets its product in the finished form. Dr. Willoughby naturally found the best illustration of this tendency in the situation of the United States Steel

Corporation; but he showed that the movement is already quite general, and is apparently destined to a much further extension. The advantages of this new system of production were shown to be considerable, the most important advantages being independence of fluctuations in the prices of materials and transportation, and the obtaining of all materials at or near the cost of production without deduction for intermediate profits. In the case of the United States Steel Corporation, moreover, it was pointed out that the greater part of its output was marketed in the form of products far removed from the unwrought steel billet, or bloom. In other words, the major portion of the earnings of the Corporation represent the combined profits of a long series of productive factors,— the mine, the coke plant, the railroad and steamship, the blast furnace, the Bessemer converter, the slabbing mill, and the plate mill,— all converging and uniting in the earnings from the sale of rails, tubes, tin plate, cotton ties, and structural material.

These gigantic profits and values, under the old-time system, before the steel industry became integrated, would have been divided among at least six classes of producers, each of which would have in turn contributed to the earnings of its predecessor, while it levied tribute upon the next in succession, and each one was at all times struggling to improve its position at the expense of its own buyers and sellers, with the result of considerable confusion of contracts and uncertainty of prices. The mine-owner could not calculate on a fixed rate of transportation; the furnace man had no certainty, beyond the limits of a single season's requirements, that he would not be mulcted in the price of ore and coke; the bridge manufacturer anxiously scanned the market prices of steel. Everywhere was ignorance, distrust, and friction. The most prominent characteristic of the interdependent system of production, as just pointed out, was the element of fluctuating costs.

Each producer in order, after a brief season of prosperity, would find his cost of production raised by the producer just before him. A high price of pig iron in the fall meant a high price of iron ore in the spring, and steel producers who had seen their customers make large profits on their purchases of low-priced billets and sheets hastened to equalize matters with these customers as soon as their commitments had been filled. As a result, no one member of the productive series was able to take full advantage of the opportunity for profits which a large consumptive demand always presents. The producer who stood nearest the consumer was perhaps in the most favorable position; but even here the manufacturer of hardware and the large buyer of materials, at the beginning of an advance of prices, eagerly contracted ahead, and the producer of tubes or wire was usually kept busy filling these low-priced contracts until the rising tide of preliminary cost destroyed his hopes of the larger profits to which high prices of his products would seem to entitle him.

At the same time that the costs of the steel industry were subject to such wide variations, the aggregate expenses of its different members suffered but slight changes in comparison. For example, the miner in the Connellsville region, during the depression in the coke trade from 1893 to 1898, received $.928 for mining 100 bushels of coal. In 1900 he received $1.25. The wages of the laborers around the ovens were changed to even less than the wages of the miner. The depreciation and sinking fund charges remained the same. The total cost of coke-making between 1897 and 1900 did not increase to exceed 25.0 per cent. per ton of coke produced, but the price of coke at the oven rose from $1.23 in 1895 to $2.70 in 1900, or 119.5 per cent.* The same can be said of the cost of ore and limestone, and also of pig iron and steel billets. The variation of the expenses of production is always much smaller than the changes in market prices, because these latter represent the changes of general demand. Price is a social fact influenced by a number of outside circumstances constantly changing in their relation and in the degree of their respective influence. The expense of production, on the other hand, is a technical fact. It measures the resistance of nature to man's efforts and the slow and gradual fluctuations of wages. Expenses of production, therefore, as compared with market prices, fluctuate within narrow limits, although their general tendency is always towards a gradual decline.

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* From information supplied by Mr. H. P. Snyder, editor of the Connellsville *Courier*.

It was from this situation of unstable costs that the "integrations" in steel production, of which the United States Steel Corporation is the foremost example, have delivered the trade; and in the freedom from the vexatious checks of advancing costs lies the explanation of the imposing profits upon which the huge capitalization of the company has been based, and to which that capitalization looks for its justification and warrant. The products of the steel trust to-day are produced at ultimate and fundamental cost,— a cost which contains hardly any element of profit from the beginning of the series to the end, and which represents only the bare expenses of producing and transporting the various materials,— ore, coke, iron, steel billet, steel plate, which antecede the final product.* These expenses of production, owing to the rapid progress of improvement in recent years at every stage of the process, are probably the lowest on record. The final products are sold at higher prices, higher than for ten years past, and in quantities which have never before been approached. The profits of the steel trust represent the total earnings at the time of its greatest prosperity of 70 per cent. of the iron industry of the United States, the combined profits of the numerous and widely sundered members of a complete productive process. These profits, if continued for five years, in spite of the heavy drain of dividend payment, will permit the accumulation of a reserve of surplus earnings sufficient in amount to guarantee the stability of both common and preferred stock.

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*No matter what system of accounting has been adopted between the constituent companies the final result would be as described.

The question at once arises, Will these profits continue? This question can be discussed from two standpoints. We can assume that the course of prices and earnings in the steel trade will follow in the future the direction of their past history, or we can accept the claim, so often made, that a new factor of potent influence has entered to steady the industrial situation and maintain the stability of industry; that the control of the supply possessed by the United States Steel Corporation will operate to steady the market, and will prevent prices from falling to the same extent as in past years. It is from the first point of view that the present discussion proceeds. The writer proposes to examine the situation of the United States Steel Corporation, on the hypothesis that a period of industrial depression, such as has invariably succeeded a period of industrial prosperity, will carry down to a low level the present prices and profits of the steel trade. An examination of the situation from the standpoint of past experience is certainly warranted, if only by the necessity of clearing the ground for the entrance of new factors, which, it is claimed, the industrial consolidations of the past four years have created.

The history of iron and steel prices is a record of fluctuations more frequent and extensive than those which have marked the course of any other class of commodities. The following table gives on four dates, covering a period of twenty years, the prices of the more important members of the group of iron and steel products:

HIGHEST AND LOWEST AVERAGE PRICES OF IRON AND STEEL, 1880–99

	1880.	1885.	1890.	1894.	1899.
No. 1 foundry pig at Philadelphia,	$28.50	$18.00	$18.40	$12.66	$19.36
Steel rails at mills in Pennsylvania	67.50	28.50	31.75	24.00	28.12

	1880.	1886.	1890.	1894.	1899
Steel billets at mills at Pittsburgh,		31.75	30.32	16.58	31.12
Wire nails of small size, Anderson, Indiana	10.40	5.91	4.60	3.81	3.28

Taking the fluctuations of pig iron as the subject of comment, we find that from 1880 to 1885 the price declined 36.9 per cent., and from 1890 to 1894 31.1 per cent., rising from 1894 to 1899 34.5 per cent. The fluctuations in the prices of the more advanced steel products were equally great. The demand for iron and steel represents perhaps more nearly than the demand for any other product the periodic fluctuations in business activity.

The course of production has tended to correspond with the range of prices. As a rule, however, although the production of iron and steel has immediately decreased in response to a fall of prices, the decline has been temporary; and within a short time, usually not exceeding a year, while prices still remain low, production has once more increased, although not at the same rate as before the decline in prices. The industries of the country having adjusted themselves to the lower level of prices, a renewed demand for iron and steel at low prices is met by an increasing supply, and normal conditions continue until the next explosion of industrial speculation sends prices up again. This sustained production of iron and steel on the new level of prices has been hitherto made possible by a readjustment of costs. The materials of every branch of the industry having fallen in price, expenses are correspondingly reduced, and a decrease in labor cost is facilitated by a decline in the cost of living. Decreasing cost of production enables the operation of works at a profit, although, without such a reduction in cost, the new price level would in most cases convert profits into losses, and cause a general suspension in the industries thus circumstanced. To put the matter concretely, unless the price of pig iron declined along with the price of steel, the steelmaker would be compelled to operate his plant at a loss. In this decline in the prices of his materials the steelmaker found partial compensation both for the decrease in his profits, resulting from the former advance in costs, and for the present decline of his selling prices. Just as the members of the productive series, beginning with the mine and the transportation company, by advancing their charges had successively raised the expenses of production of the later stages of the process, so now, beginning with the manufacturer of finished materials and reversing the order, prices and costs successively declined. The wire mill paid less for rods, the rod mill for billets, the steelmaker for pig iron, until the weakness in demand from the final consumer had passed from one stage to the other back to the railroad, the boat, and the mine. The result of the interdependence of industry in a time of falling prices was, therefore, a compensating decline of the expenses of production, and a reduction of profits relatively much smaller than would have been the case, had costs of production remained comparatively stable from the beginning. While the aggregate profits of an interdependent industry over an extended period, compared with those of an integrated industry, are much smaller, they are, for the foregoing reasons, more evenly distributed, and exhibit in their movements a small margin of variation.

The significance of this principle of profit variation as applied to determine the security of the steel stocks is as follows: The United States Steel Corporation is an integrated industry. Its expenses of production contain but few elements of profit, and, compared with those of the régime which it superseded, are relatively stable. Its aggregate profits are, therefore, much larger; but, on the other hand, they are more unevenly distributed,— that is to say, the margin between the high and low points of the profit curve is much greater than if the Corporation was obliged to purchase its supplies from other producers. In capitalizing the profits of such an integrated industry, the amount of stocks and bonds that can safely be issued should not absorb the maximum earning power of the new company, but should preferably represent the average of high and low profits, or, even more prudently, should be fixed at a point where the requirements of interest, maintenance, and dividends should not absorb more than the minimum earnings. If both of these rules are disregarded, and the maximum earnings of an integrated company are fully capitalized, especially if the capitalization contains a large proportion of interest-bearing obligations, its financial standing is certain to be impaired by the first decline of prices. A conservative policy is evidently far more necessary in the capitalization of an integrated than of a non-integrated company, because, in the case of a non-integrated business, the proportionate decline in profits, as a result of a fall in prices, is much less than where little compensation for falling prices is afforded by decreasing cost of materials. It is, therefore, impossible to escape the conclusion that the stocks of the United States Steel Corporation, because its capitalization is based upon the maximum profits of an integrated industry at a time when the margin between costs and prices was the widest, and also because that capitalization contains a considerable element of bonded debt, will be in danger of serious depreciation if prices should follow the course of past years.

It may be of interest to follow the working out of this principle of profit variation in a concrete case. The writer was recently privileged to examine a confidential report on the financial history of a prominent blast furnace company, which presented a detailed record of costs, selling prices, production, and earnings for a series of years. This company contracted for all its materials.

The management, equipment, economy, and efficiency of operation of this company have always been of the highest order. In fact, it is generally recognized as one of the best of the independent furnace companies in the State in which it is located. The main facts of its financial history are presented in the following table: —

Year.	*Price of Iron per Ton.*	*Cost of Materials.*	*Profit per Ton.*	*Annual Production, Tons.*	*Net Earnings.*
1890 . .	$15.74	$12.70	$2.00	39,659	$67,928.29
1891 . .	14.57	12.29	1.24	37,589	39,072.96
1892 . .	13.63	11.73	.86	30,755	18,244.77
1893 . .	12.31	10.27	1.00	50,957	25,787.98
1894 . .	10.58	8.82	.72	51,163	13,714.77
1895 . .	10.74	8.67	1.03	53,932	42,971.86
1896 . .	11.29	9.44	.71	37,107	20,815.94
1897 . .	10.40	8.55	.81	63,137	33,150.57
1898 . .	9.79	7.99	.76	64,816	32,319.51

The proposition which has been laid down regarding the tendency of the costs of non-integrated industry to vary with its profits is substantiated by this record. Compare, for example, the variation in the selling price of pig iron from 1890 to 1894 with the change in the tonnage cost of materials during the same period. A fall in price of $5.16 is largely offset by a decline in cost of materials of $3.88; and, as a result of this decline in materials, a profit is still earned. Had it not been for this fall in the price of ore and coke, the company would have sustained a heavy loss after 1893; for the selling price of pig iron from 1894 to 1898 was less than the cost of materials in 1890.

Let us now suppose that the proprietors of this company in 1890, the year of highest profits, corresponding to the year 1901, had decided to capitalize their enterprise on the same basis as that on which the capitalization of the United States Steel Corporation has been issued, namely: 5 per cent. bonds, 21.4 per cent. of the total; 7 per cent. cumulative preferred stock, 44.3 per cent.; and common stock, 44.3 per cent. Let us further assume that, just as the steel trust has done, the new company decided to set aside 11.2 per cent. of its net earnings for sinking fund and maintenance charge, or $7,607.96 out of net earnings of $67,928.29, as well as a surplus reserve equal to 40 per cent. of net earnings, or $27,171.32, before capitalizing any part of their income. The promoters of the iron company, pursuing the same policy of maintenance, sinking fund, and surplus reserve charges as that adopted by the promoters of the United States Steel Corporation, would have had remaining $33,149.01 of the net earnings of 1890, upon which to base their issues of stocks and bonds. Indeed, this apportionment of earnings is even more conservative than that adopted by the syndicate managers of the steel trust; for it was not expected that the earnings of the consolidation would much exceed $100,000,000. That is to say, putting the matter in another form, the proportion of surplus reserve which our supposed corporation in 1890 desired to set aside was at least 60 per cent. larger than the original intention of the organizers of the steel trust in this regard.

On this relatively conservative basis, and apportioning the available net earnings of the (———) Iron Company among the three classes of securities in the same proportions as the steel trust has apportioned its earnings, we have the following capitalization in 1890, corresponding to the capitalization of the United States Steel Corporation in 1901, and bearing the same relation to the net earnings of that company: —

Class of Security.	*Principal.*	*Interest or Dividends.*
7% cumulative preferred stock	$237,725.60	$16,640.79
4% common stock	276,160.00	9,846.00
5% bonds	133,258.98	6,662.44
	$647,144.58	

We now have our company organized on the same basis, in relation to the surplus reservation out of its earnings of 1890 and the capitalization of the different classes of securities, as the United States Steel Corporation in 1901. It will be instructive to follow the fortunes of our new company through the nine years succeeding its organization; and this is done in the following tables, which give (1) net earnings, (2) requirements for interest maintenance and dividends, and (3) surplus account from 1890 to 1898.

	I.	II.	III.	IV.	V.
YEAR.	Net earnings.	Fixed charges.	Fixed charges + 7 per cent. on preferred stock.	(III.) + 4 per cent. on common stock.	Surplus (+) or deficit (—).
1890	$67,928.29	$17,453.96	$34,094.75	$40,757.69	+27,170.60
1891	39,072 96	"	"	"	— 1,684.73
1892	18,244.77	"	"	"	—32,512.92
1893	25,787.98	"	"	"	—14,969.71
1894	13,714 77	"	"	"	—27,042.92
1895	42,971.86				+2,214.17
1896	20,815 94	"	"	"	—19,941.75
1897	33,150.57	"	"	"	—17,607.12
1898	32,319.51	"	"	"	—18,438.18

We have here represented the financial history of a company capitalized on the same basis as the United States Steel Corporation during a period of low prices. Let us go over the results appearing in column "V.," applying them to the position of the different securities, and assuming that the Corporation is managed with an eye to security. In 1890, after meeting all fixed charges and paying dividends on both preferred and common stock, a handsome surplus would have remained on the year's operations. In 1891 the surplus of the preceding year would have been trenched upon to the extent of $1,684.73 to keep up the common stock dividend. In 1892, no dividends could safely be paid on either class of stocks, because, after meeting fixed charges, only $790.81 remained out of the net earnings of the year. This would be added to the surplus reserve, bringing that item up to $27,286.68. In 1892, since the preferred stocks are cumulative, a back dividend of 7 per cent. is accumulated, which must be paid before dividends are resumed on the common stock. In 1893, to continue our examination, $8,334.02, or 3½ per cent., was earned on the preferred stock. In view of the fact that the surplus reserve of the company, which now stands, as above noted, at $27,286.68, is only 4.4 per cent. of the total capitalization, a prudent management, such, for example, as the present governing body of the United States Steel Corporation, would undoubtedly refuse to pay out this excess of net earnings over fixed charges, and would carry the balance to surplus, bringing that account up to $35,620.70. The consequence of this decision would have been to add another 7 per cent. to the accumulation of unpaid preferred dividends already standing against the common stock. In 1894, came the period of low prices, which would have justified the conservative decision of the preceding year. Net earnings would have fallen below fixed charges, and $3,745.19 would have been drawn from the reserve to pay interest, bringing down the reserve to $31,875.51. Another passed dividend on the preferred would have accumulated 21 per cent. against the common stock. The result of the operations of the next four years would have been a surplus of $59,442.04 over the total fixed charges for this period. Out of this sum, 3½ per cent. could have been safely paid on the preferred stock, and the balance, $26,160.46, carried to surplus reserve, increasing that account to $58,035.97, which is 4 per cent. on the capitalization of the company,— a very respectable showing, although still considerably less than the highest standard of investment security would have required. By 1898, however, the accumulation of back dividends against the common stock would have amounted to 35 per cent. on the preferred stock; and the junior security, therefore, would have only a nominal value, not merely in view of the existence of the back claim accumulating for eight years past upon future earnings, but because of the fact that no dividends had been paid for an extended period upon the common stock. The value of the preferred stock would have probably settled itself around 40, and the bonds alone would rank as an investment security. The conclusion is plain that the basis of capitalization of the United States Steel Corporation, if the experience of the (———) Iron Company is any criterion, and if prices follow the course of past years, is dangerously insecure, and that both classes of stocks are at all times highly speculative in character.

The financial analogy which has been drawn, however,* is by no means complete. The profits upon which it is based are those of a non-integrated company that found a large measure of compensation for the decline in the price of its product in the reduced value of its materials. The high and low points of the profit curve of the (———) Iron Company are, therefore, much less widely separated than would have been the case, had the company produced its own materials instead of purchasing these from other producers. In order to make an exact parallel with the present situation of the United States Steel Corporation, it is necessary to reestimate the earnings of the company under examination on the basis of a cost price for materials. In making this estimate, the average cost of materials to the company from 1894 to 1898 is taken as an approximation of the total expenses of producing these materials from 1890 to 1893. This estimate is probably somewhat under the facts, but, as will presently appear, is all the more warranted for that reason. Taking materials at producers' cost, just as the United States Steel Corporation receives them, the profits of the (———) Iron Company in 1890 would have been $228,039.25 instead of $67,928.29, the amount actually realized; and the capitalization of the company, arranging it as before on the basis of the same allowance of surplus and maintenance charges, and with the same apportionment of earnings to the different classes of securities as the method employed in the capitalization of the United States Steel Corporation, is as follows: —

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* The writer has not been able to obtain a statement of the earnings of the (———) Iron Company from 1898 to 1901. He has been informed that full advantage was taken of the recent rise of prices, and that the large earnings of 1890 were considerably exceeded in these later years. The inference is that, even on the assumed basis of capitalization, the back dividends could have been paid off out of the profits of two years operations, and that during the past two years the company could have paid a good dividend on its common stock. This favorable result, however, does not in any way authorize the scale of capitalization which has been mentioned.

INCOME.

Total net earnings	$228,039.25
Reserved for surplus	72,960.00
Reserved for sinking fund and maintenance	28,280.00
Available for fixed charges and dividends	126,760.70

CAPITAL AND CAPITAL REQUIREMENTS.

	Principal.	*Interest and Dividend Requirements.*
5% bonds	$527,136.00	$26,356.80
7% cumulative preferred stock	908,091.00	63,566.40
4% common stock	920,937.60	36,837.50
Totals	$2,356,164.60	$126,760.70

Here is a capitalization, based upon the earnings of an integrated industry for 1890, and apparently warranted by those earnings, nearly four times as great as the capitalization which could be based upon the earnings of a non-integrated industry after allowing the same proportion of reserve. The enormous preponderance in earnings of the modern system of production represented by the steel trust, compared with the old-fashioned method, is at once apparent. But the danger of a full capitalization of these larger earnings is equally evident. For now we are to have but little compensation for declining prices in declining costs. Let us admit a decline in producers' cost from 1890 to 1894 of 20 per cent., which is certainly well above the reduction that actually took place, and see how our company stands the strain. The statement of earnings, fixed charges, dividend requirements, and surplus account,— taking materials at producers' cost,— would have been as follows: —

Year.	*Net Earnings.*	*Fixed Charges.*	*Fixed Charges + 7% on Preferred Stock.*	*(III.). 4% On Common Stock.*	*Surplus* (+) *or Deficit* (—).
1890	$228,039.25	$59,636.80	$118,203.20	$155,040.00	+ $72,960.00
1894	21,488.46	59,636.80	118,203.20	155,040.00	— 133,551.54

In sharp contrast with a surplus over all requirements of $72,960 in 1890 appears a deficit of $38,148.34 below fixed charges in 1894; and from this time on fixed charges would have more than absorbed all available revenue, leaving nothing for surplus and for the preferred stock, and considerably less than nothing for the common stock, which would have been buried under a mountain of preferred accumulations. In other words, before the period under examination had been half concluded, the property of our company would have been in the hands of the bondholders. Such would have been the inevitable result of putting the (——) Iron Company in control of the sources of its supplies of material in 1890, and of capitalizing the larger earnings thence resulting on the same basis as that on which the present capitalization of the United States Steel Corporation is based.

The lesson of this analogy and its application to the situation of the United States Steel Corporation is by no means obscure. It has already been plainly stated, but will bear repetition. The steel trust has capitalized to the full limit of present safety the largest earnings in the history of the steel trade. The surplus which will remain out of the earnings of the current year is no more than sufficient to meet the requirements of investment security.

If these earnings continue for five years, as has been pointed out, a reserve of approximately 15 per cent. will have been accumulated, and the Corporation can begin to plume itself on its investment standing. If prices and earnings in the steel trade, however, follow the same course as in past years, those earnings will suffer a decline more astonishing than their advance has been phenomenal. The proposition cannot be too often emphasized that integrated industry means more stable cost of production, and therefore, unless an equal stability can be imparted to the prices of sale and the volume of output, a wider zone of profit variation. With integrated industry, costs do not rise with prices; and profits, therefore, increase with greater rapidity than when other profits are deducted from them. But, on the other hand, when the turn comes and the tide of prosperity ebbs, since the expenses of production have not risen with the advance, neither do they decline with the depression; and prices fall with slight compensation from decreasing costs. The capitalization of the steel trust represents the top of the wave of prosperity. It is not difficult to forecast the value of that capitalization when the wave recedes.

It is not the writer's purpose to venture upon a prediction of disaster to the Steel Corporation. If steel prices and the earnings of the steel trade decline, as they always have declined in the past, there cannot be the slightest question that the value of both issues of its capital stock will be destroyed, with every probability that title to its properties will pass to the holders of its mortgage bonds. This is the teaching of experience. Steel has always been, in the picturesque phrase of Mr. Carnegie, either a "king or a pauper." And poverty in the steel trade means the extinction of the steel trust. It is, however, legitimate to urge that industrial conditions, as a result of the inevitable consolidations of recent years, are now so stable that the earnings of the Steel Corporation can be maintained on a high level. This opinion has the sanction of high scientific authority, and it is not to be lightly gainsaid. It will be fortunate for the holders of the steel stocks if the result shall justify these optimistic predictions.

As this paper goes to press, the second report of the Steel Corporation shows estimated net earnings for the first year of $100,000,000, a considerable reduction from the original estimate of $125,000,000 adopted as the basis of the preceding computations. The result of a re-computation would evidently be much less favorable to the Corporation than the one which is allowed to stand.

EDWARD SHERWOOD MEADE.

UNIVERSITY OF PENNSYLVANIA.